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**Before the  
FEDERAL COMMUNICATIONS COMMISSION  
Washington, DC 20554**

In the Matter of

Access Charge Reform and  
Pricing Flexibility

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)  
CC Docket No. 96-262;  
CC Docket No. 94-1; RM-9210

FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF THE SECRETARY

**REPLY COMMENTS OF THE  
COMPETITIVE TELECOMMUNICATIONS ASSOCIATION**

**THE COMPETITIVE  
TELECOMMUNICATIONS  
ASSOCIATION**

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## SUMMARY

The fundamental assumption of the Commission's market-based approach in the *Access Charge Reform Order* is that the advent of local competition will create downward pressure on ILEC switched access charges. As CompTel and numerous other commenters showed, local competition – and more importantly, *access competition* --has not developed as the Commission predicted. Therefore, the Commission's market-based approach must be reexamined to produce reasonable access rates in the near term. In its initial comments, CompTel recommended that the Commission accelerate its prescriptive backstop and prioritize reductions in access rates over a two-year transition period beginning July 1999.

The beneficiaries of the current above-cost rates – the price cap LECs – object to this approach on three grounds, none of which have merit. First, not surprisingly, the price cap LECs are quite happy with the pace of local competition, and claim that it is too early to conclude that market forces will not constrain interstate switched access charges. However, as vividly demonstrated by the Commission's five orders denying BOC Section 271 applications for interLATA authority, local competition simply has not arrived at this point. Substantial setbacks such as the Eighth Circuit's rulings regarding the provision of UNEs that already are combined have undermined the ability of competing carriers to provide broad-based local exchange services, and have increased the cost and complexity of local entry. More importantly, even if patience is called for with respect to *local competition*, the Commission must understand that the presence of competition for end users of local services does not necessarily create incentives for competition for carriers using access services. Local exchange and exchange access services are two different services with different customers and different market dynamics. The existence of competition in one (local exchange) does not mean that there will be

competition in the other (exchange access). Indeed, the price cap LECs offer no evidence that *access competition* has increased since the *Access Charge Reform Order*.

Second, the price cap LECs claim that per-minute access rates are declining, and that price cap regulation is working adequately to lower access rates. However, the fact that virtually all LEC access rate elements are at the price cap indices demonstrates that the price cap regime has lowered access rates only through its mandatory mechanisms, not through competitive pressures. While the trend certainly is in the correct direction, reliance on price caps alone will take over two decades to reach forward looking costs, even if the ILECs' attempts to slow the pace of price caps are rejected (as they should be). This is simply too long to allow consumers to continue to bear the burden of excessive access charges. The appropriate target has already been determined by the state PUCs in their decisions establishing UNE rates; the Commission should move access rates toward those levels without delay.

Third, price cap LECs trot out the discredited argument that above cost access rates are necessary to promote other goals, principally, maintaining universal service and promoting facilities deployment. However, the Commission is *separately* addressing universal service needs, establishing a mechanism from the ground up, rather than shifting dubious alleged "subsidies" from various sources. In any event, the Commission has nearly completed its reform of the universal service high cost support mechanisms, and CompTel supports completing that job promptly this Spring, *before* prescriptive access reforms would take effect. In addition, there is no reason to maintain access above cost, as the price cap ILECs argue, in order to encourage others to deploy their own facilities. The Commission has long recognized that *efficient* prices provide the proper incentives for deployment of facilities, without economic distortions caused by above-cost pricing.

Accordingly, CompTel urges the Commission to move promptly to bring access charges to their forward-looking costs. CompTel's Prescriptive Transition Plan properly prioritizes access rate reductions and should be adopted by the Commission.

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COMPETITIVE TELECOMMUNICATIONS ASSOCIATION**

The Competitive Telecommunications Association ("CompTel"), by its attorneys, respectfully replies to the comments filed in response to the *Public Notice* released on October 5, 1998.<sup>1</sup> For the reasons explained below, the Commission should not allow the price cap LECs' objections to stand in the way of a prompt transition to cost-based access rates.

**I. INTRODUCTION**

There is little dispute regarding the proper goal of the Commission's access charge policy. The Commission has already concluded – and no party seriously urges otherwise – that access rates should be priced to reflect forward-looking costs of providing service.<sup>2</sup> The only issue is how to reach that goal – and how quickly the Commission should get there.

In its comments in response to the *Public Notice*, CompTel showed that the fundamental assumption underlying the Commission's market-based approach thus far has not materialized.

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<sup>1</sup> *Commission Asks Parties to Update and Refresh Record for Access Charge Reform and Seeks Comment on Proposals for Access Charge Reform Pricing Flexibility*, FCC 98-256 (Oct. 5, 1998) ("*Public Notice*"). Initial comments were filed on October 26, 1998.

<sup>2</sup> *See In re Access Charge Reform*, 12 FCC Rcd 15982, 16097 (1997) (subsequent history omitted), *aff'd sub nom. Southwestern Bell Tel. Co. v. FCC*, 153 F.3d 523 (8<sup>th</sup> Cir., Aug. 19, 1998) ("*Access Charge Reform Order*").

Impediments to broad-based local entry have undermined the Commission's reliance on competition in local exchange services to unleash competitive pressures to lower switched access rates. Moreover, even if competition in *local exchange* services could be jump-started, such competition does not automatically or easily translate into *access charge* competition. In short, the "market-based" approach is not working today, and it is unclear at this time whether it can ever be revived. As a result, access charges remain significantly above their forward-looking costs.

The Commission must now re-evaluate its approach in light of these changes. CompTel proposed in its comments that the Commission accelerate its prescriptive reforms by establishing specific deadlines for access charges to be set at cost-based levels. CompTel proposed a Prescriptive Transition Plan which prioritizes access reform, beginning first with those access rate elements which are not now, and are not likely to become, subject to any significant competitive pressures, and completing the transition over a two year period.<sup>3</sup>

The beneficiaries of today's excessive price structure – the price cap LECs – raise three objections to this approach. First, they claim that the market-based approach is working fine, albeit slower than the Commission might have anticipated. They urge the Commission to continue to wait to see if its theory might work. Second, the price cap LECs argue that access rates have been declining and assert that price cap regulation is reducing access rates. Finally, they argue that above-cost access rates should be preserved in order to promote other goals, including maintaining universal service and promoting facilities deployment. As shown below, all three of these objections are without merit.

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<sup>3</sup> CompTel Comments at 13-14.

## II. IT IS NOT TOO EARLY TO CONCLUDE THAT CIRCUMSTANCES HAVE INTERVENED TO THWART THE COMMISSION'S DESIRE TO RELY ON MARKET FORCES

The Commission's *Access Charge Reform Order* chose to rely on market forces, rather than regulatory prescription, to bring LEC access charges in line with the cost of providing access services. As CompTel showed in its comments, those market forces have not developed. This assessment is confirmed by the comments of those entities that the Commission expected would bring that competition to the market. For example, AT&T notes that the "factual assumptions underlying the market-based approach previously proposed by the Commission have subsequently become invalid."<sup>4</sup> This situation flows in part from the fact that, as MCI WorldCom indicates, "the industry has been sidetracked by seemingly endless litigation and incumbent intransigence in complying with their statutory duties to provide competitors" the ability to compete against them.<sup>5</sup> Moreover, there is no evidence that broad-based local competition will develop in the near future.<sup>6</sup>

The price cap LECs, however, argue that the market is working, albeit slowly. USTA asserts, for example, that there has been "dramatic growth in competition from competitive LECs" in the past year.<sup>7</sup> Quoting generously from Wall Street analysts' predictions, USTA paints a particularly rosy view of CLECs' *prospects*. USTA ignores the fact, however, that local competition remains in its infancy. CLECs have been denied cost-effective, efficient means to serve customers through the use of ILEC UNEs. Moreover, no ILEC has deployed the OSS and other "back office" functions sufficient to support high volumes of local service changes. As a

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<sup>4</sup> AT&T Comments at 8.

<sup>5</sup> MCI WorldCom Comments at 18.

<sup>6</sup> *Id.*

<sup>7</sup> USTA Comments at 6-8.



result, broad-based competition is non-existent, and CLECs remain confined to the geographic areas where they have deployed their own facilities. As has been noted many times before, despite the massive efforts of CLECs to deploy such facilities rapidly, replication of the ILEC network in the short term simply is not possible. Thus, while CompTel continues to work toward making competition a reality, the truth is that the road ahead of us is much longer than the road behind us.

Importantly, the development of local competition, while necessary, is only the first step required under a market-based approach to access reform. Even if local competition were to emerge, or if such competition could be jump-started, market pressures are unlikely to drive access charges to cost-based levels. When local competition develops, a local exchange carrier will have an incentive to lower the total charges for its service to end users, but this incentive will fail to place any downward pressure on the rates charged to third-party IXC's for access to the customer.<sup>8</sup> This problem is particularly acute in the context of terminating access services, where the calling party has no ability to choose the terminating access carrier, and in the context of tandem-switched transport, where no competition to the incumbent LEC has yet emerged. Thus, even if the price cap LECs' claims regarding the state of local competition were correct, local competition would not easily translate into appreciable reductions in switched access rates.

In contrast to their rosy predictions of future local competition, the price cap LECs have produced no evidence that there is competition in the switched access market. This is the area where the FCC must see at least some progress toward competition if the market-based approach for *access reform* is to work. But no such competition is visible today. For example, neither

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<sup>8</sup> Indeed, AT&T recently petitioned the Commission claiming that switched access charges by *non-ILEC* local carriers often exceed the incumbent's access rates. AT&T, Petition for Declaratory Ruling, filed Oct. 23, 1998.

USTA nor any other LEC identifies any carriers that are competing to provide switched access services, including tandem-switched services on which many CompTel members rely. Nor are there any signs that the price cap LECs are responding to competitive pressures in setting their switched access rates. As AT&T noted in its comments, virtually all switched access rate elements are priced equal to the applicable price cap index.<sup>9</sup> This strongly suggests that, without acceleration of the prescriptive approach, access rates will remain well above their forward-looking costs.

For these reasons, it is not premature to judge the effectiveness of the Commission's market-based approach. It has been seventeen months since the Commission adopted the *Access Charge Reform Order*. In that time, experience has demonstrated that the market based approach either will never bring access charges to cost, or that, if it will, it will not do so for a very long time. Under these circumstances, the Commission should reconsider its approach.

### **III. EXISTING MECHANISMS TO LOWER ACCESS CHARGES ARE NOT WORKING FAST ENOUGH**

Related to the first argument, the price cap LECs argue that the Commission should wait while its price cap mechanisms further reduce access charges. Access charges have been declining under price caps, they argue, and therefore the Commission need only allow that mechanism to continue to operate.<sup>10</sup> However, the Commission already knows that access charges are far above cost today, and it knows that the goal is to reduce those charges to cost. It should not delay – whether for price caps or for other reasons – in moving to achieve that goal.

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<sup>9</sup> AT&T Comments at 5 n. 7.

<sup>10</sup> See, e.g., USTA Comments at 3-4.

First, to the extent that price caps have lowered access charges, it is due to the application of the Commission's adjustments to the price cap indices themselves, not to competitive pressures or incentives to reduce costs. With access charges set at the applicable price cap indices,<sup>11</sup> reductions in access rates result from operation of the productivity factor (the so-called "X-factor") to lower the relevant index. Yet, at the same time that these parties point to the effects of this element of the price cap mechanism, they are attempting to halt that decline by lowering the productivity factor.<sup>12</sup> The fact that access rates track the price cap index is a reason to increase the prescriptive effect of the Commission's rules, in order to increase the pace at which access charges are reduced to forward-looking costs. If the LECs are not voluntarily lowering access charges when price caps give them significant downward flexibility, the Commission needs to mandate reductions in access charges.

Second, other portions of the reduction in the per-minute rate are the result of shifting – not eliminating—some access charges to the SLC or PICC. Price cap LEC access revenues are not lowered by this action, they are merely recovered from carriers and customers in a different way (and with a disproportionate impact on small business users). It appears, for example, that the majority of the reduction in the per-minute access charge that USTA predicts will occur through 2003 is the result of increasing the PICC, not of an actual reduction in access revenues.<sup>13</sup> Thus, the extent to which the current price cap mechanism will lower access charges is overstated.<sup>14</sup>

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<sup>11</sup> AT&T Comments at 5 n. 7.

<sup>12</sup> See, e.g., USTA Comments at 20.

<sup>13</sup> *Id.* at 4.

<sup>14</sup> During the transition to cost-based access charges, the Commission should not allow any interim increases in access rate elements – including the PICC and transport-related charges—that currently exceed costs.

Third, the issue is not where access charges used to be, but where they are now, and where they are going. Despite the reductions attributed by the LECs to price caps, interstate switched access charges remain well above their forward-looking costs. State commission approved interconnection rates demonstrate that the ILECs' forward-looking cost of providing transport and termination for local calls – a function identical to access – is below one half of one cent (\$0.005) per minute. Price cap LEC access charges – originating or terminating --currently are over three times that level – generally equaling approximately \$0.017 per minute. At the current productivity factor, all else remaining the same, it would take decades for access charges to be reduced to cost-based levels.<sup>15</sup> This is simply too long to wait for reasonably-priced interstate switched access.

On a related note, some LECs argue that the Commission should not accelerate its prescriptive backstop to access reform because that action allegedly is “inconsistent” with the rationale of price cap regulation. The prescription of cost-based access, these LECs contend, is a step backward from price cap regulation to the rate of return principles the Commission abandoned in favor of price caps.<sup>16</sup> Prescription based upon state-determined TELRIC interconnection rates is not equivalent to reimposing rate of return regulation. Rather, TELRIC-based pricing “best replicates, to the extent possible, the conditions of a competitive market.”<sup>17</sup>

When the Commission moved away from rate of return regulation for the largest LECs, it identified three inefficiencies associated with that regime. First, because a carrier can pass almost any cost along to the ratepayers, it does not have an incentive to innovate or use equipment or

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<sup>15</sup> Using an extremely conservative cost estimate (*i.e.*, erring on the high side) of \$0.005 per minute, would take 19 years for the existing 6.5 percent productivity factor to force the per minute rate to cost.

<sup>16</sup> See, *e.g.*, BellSouth Comments at 8-9; U S West Comments at 3.

services in an efficient manner. Second, there is an incentive to cost-shift away from unregulated activities and toward regulated ones. Third, it is costly to administer rate of return regulation due to the constant need to calculate and allocate the carriers' costs.<sup>18</sup> None of these concerns apply to the TELRIC-based prescriptions CompTel advocates.

First, TELRIC pricing is based upon the forward-looking costs of an efficient provider. Thus, a carrier would not have an incentive to increase its costs, or to shift costs from nonregulated accounts to regulated accounts. Second, administration of a TELRIC approach is significantly simplified by its reliance on efficient costs. Indeed, USTA consultant Taylor's concerns about the burdens of prescriptive pricing upon the Commission are largely obviated by the fact that, in this case, the necessary studies have already been conducted by the states.<sup>19</sup> Therefore, there is little additional review that the FCC needs to conduct to apply these rates to interstate switched access charges.

Finally, the price cap LECs also trot out their time-worn arguments that TELRIC pricing itself is difficult or an inappropriate standard.<sup>20</sup> The FCC has repeatedly rejected these claims, and it should do so again. In the *Local Competition Order*, the Commission explicitly rejected the ILECs' argument that TELRIC pricing is inherently hypothetical and impractical. To the contrary, forward-looking "approaches are practical and implementable."<sup>21</sup>

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(...continued)

*Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, 11 FCC Rcd 15499, 15846 (1996) ("Local Competition Order").

<sup>18</sup> See *Policy and Rules Concerning Rates for Dominant Carriers*, 5 FCC Rcd 6786, 6789 (1990) ("LEC Price Cap Order"), *recon.*, 6 FCC Rcd 2637 (1991), *further recon.*, 6 FCC Rcd 4524 (1991), 7 FCC Rcd 5235 (1992), *aff'd sub nom National Rural Telecom Ass'n v. FCC*, 988 F.2d 174 (D.C. Cir. 1993) ("National Rural Telecom").

<sup>19</sup> USTA Comments at Attachment B.

<sup>20</sup> See, e.g., U S West Comments at 13; GTE Comments at 16.

<sup>21</sup> *Local Competition Order* at 15847.

#### **IV. THERE ARE NO POLICY REASONS TO MAINTAIN ABOVE-COST ACCESS RATES**

Continuing their pattern, incumbent LECs again preach the virtues of above-cost pricing, predicting a series of dire consequences if access rates are reduced to cost too quickly. Chief among these are the claims that above-cost access rates are necessary to protect subsidies allegedly used to support universal service and that cost-based pricing will eliminate incentives for other carriers to deploy their own facilities. Both of these arguments are unsound and should be rejected. Put simply, there is no public policy reason to allow price cap LECs to continue to overcharge consumers by three times their cost in providing switched access services.

Regarding universal service reform, CompTel agrees that the Commission should promptly complete its process of establishing an explicit universal service support funding mechanism for high-cost support. But this is not a reason to slow access reform. Universal service reform is proceeding from the ground up, with the Commission establishing an explicit mechanism to calculate the needed support independent of alleged implicit subsidies that may exist in access or other rates. This process is already set in motion and, indeed, is nearly complete. The Commission has established the basic parameters of its support mechanism, and selected the cost model that will be used to calculate support. The only action left, which is scheduled to be completed this Spring, is to determine the specific cost factors and other inputs that will be used in this model. One of the benefits of promptly completing those tasks is that it will free the Commission to concentrate on the merits of reforming access charges without the distraction of the ILECs' Chicken Little claims regarding the impact on universal service.<sup>22</sup>

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<sup>22</sup> Importantly, the current access charge structure and rate levels grew from a number of factors, and the connection between excessive switched access rates and universal service high cost support is tenuous and ill-defined at best. The only thing that is certain is that access is priced well above cost. Nevertheless, CompTel's proposed transition plan  
(continued...)

In addition, there is no reason to maintain access above cost, as the price cap ILECs argue, in order to encourage others to deploy their own facilities.<sup>23</sup> The Commission has long recognized that *efficient* prices provide the proper incentives for deployment of facilities, without economic distortions caused by above-cost pricing. TELRIC pricing “will best ensure the efficient investment decisions and competitive entry contemplated by the 1996 Act.”<sup>24</sup> Thus, prompt reduction of switched access charges to forward-looking costs will send the proper signals to the market, and encourage the efficient deployment of facilities by competing carriers.

For these reasons, prompt reduction of access charges to forward-looking costs should not be sacrificed in the name of other policy goals. Efficient, cost-based access charges send the proper price signals to the market, and will encourage competition for end user telecommunications services. Maintaining above-cost access charges will subject consumers to higher rates, with no benefit toward other goals.

**V. PRICING FLEXIBILITY PROPOSALS SHOULD NOT BE CONSIDERED UNTIL AFTER ACCESS CHARGES ARE AT COSTS AND A COMPETITIVE MARKET HAS DEVELOPED**

Several LECs repeat their requests for “pricing flexibility” in access charges.<sup>25</sup> Although the features of each proposal differ slightly, particularly in the “trigger” that justifies additional flexibility, the proposals share the erroneous premise that “flexibility” will promote reductions in access rates. But flexibility at a time when access is well above cost and in the absence of real

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(...continued)

begins to reduce access charges shortly *after* the Commission is expected to complete its high-cost fund, and reduces switched access charges in phases, eliminating any alleged impact on universal service.

<sup>23</sup> SBC Comments at 33-34; USTA Comments at 16-18.

<sup>24</sup> *Local Competition Order* at 15858.

<sup>25</sup> *See, e.g.,* Bell Atlantic Comments at 16-17.

exchange access competition will only serve to increase price cap LECs' opportunities to discriminate among carriers or customers.<sup>26</sup>

The types of pricing flexibility advocated by the LECs are fundamentally inconsistent with above-cost access rates. As long as rates are significantly above forward-looking costs, and access competition is non-existent, a prescriptive approach is needed to reduce access to cost. Pricing flexibility can undermine the effect of a prescriptive approach, however, because LECs can manipulate pricing to slow the pace at which they reduce access to cost-based levels. Pricing flexibility in this context only means that some carriers will pay rates well above cost (because they have no choice), while rates can be lowered (but still above cost) to thwart efforts to provide choices for other carriers. Discrimination in this manner will not reduce access rates to cost, nor will it promote a market environment where competition might bring access to cost.

Rather than granting this type of pricing flexibility, the Commission should focus on achieving cost-based access rates. If that is achieved, and if a competitive market does develop, then the Commission should examine ways it can reduce or eliminate pricing restrictions.

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<sup>26</sup> See ALTS Comments at 6.



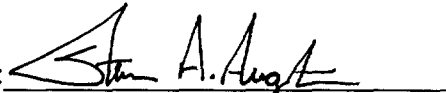
## CONCLUSION

For the foregoing reasons and for the reasons explained in CompTel's October 26, 1998 comments, the Commission should accelerate its prescriptive backstop in order to transition access charges to cost-based levels. CompTel's Prescriptive Transition Plan provides a rational way to reduce access charges to cost promptly, and based upon reasonable priorities. Accordingly, the Commission should require incumbent price cap LECs follow the implementation schedule described in CompTel's comments to bring access charges to forward-looking economic levels over the next two years.

Respectfully submitted,

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## CERTIFICATE OF SERVICE

I, Patricia A. Bell, hereby certify that on this 9<sup>th</sup> day of November, 1998, I caused true and correct copies of the foregoing **"Reply Comments of the Competitive Telecommunications Association"** to be served via hand delivery upon the individuals listed below.

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